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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 365

NOAH ADAIR,

Petitioner,

vs.

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, A NATIONAL BANKING ASSOCIATION.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

PETITIONER'S SUPPLEMENTAL BRIEF.

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PETITIONER'S SUPPLEMENTAL BRIEF.

Question Involved.

The sole question involved in this case is whether petitioner, Noah Adair, appointed Conciliation Commissioner by the United States District Court, could use part of the proceeds of a mortgaged crop of grapes for the purpose of conserving the bankrupt's estate for the benefit of respondent, Bank of America National Trust and Savings Association, the mortgagee—and for other creditors.

The proceeding here is under Section 75 of the Bankruptcy Act. The United States District Court sat as a Court of Equity and the general principles that, "He who seeks equity must do equity" or "He who comes into equity must come with clean hands", applies. The attempt to get

something for nothing at the expense of another, because of legal technicalities, never has and never will succeed in a Court of Equity.

"Equity regards substance and not form." "It regards that done which ought to have been done." In short a Court of Equity uses common horse sense and does justice between the parties on the broad principles of right and wrong. We concede that it does this within well-established rules of practice and procedure.

Argument.

The petitioner, Noah Adair, during the time here in question was the duly appointed and acting Conciliation Commissioner for San Bernardino County, California. A Conciliation Commissioner, under the provisions of Section 75 of the Bankruptcy Act, is a judicial officer of the Court. He and the farm owner perform the functions and duties of a trustee in bankruptcy. (Subsections (e), (n) and (o), Sec. 75.) (*Robert Page Wright* v. *Vinton Branch of the Mountain Trust Bank of Roanoke, Va., et al.*, 300 U. S. 440.)

On August 4, 1934, Andrea Cuccia, a farmer in San Bernardino County, filed his petition under Section 75 of the Bankruptcy Act. This petition was approved on August 6th by the United States District Court for the Southern District of California and referred to the petitioner, Noah Adair, as Conciliation Commissioner (R. 18).

We concede that the respondent bank had a real estate mortgage on the bankrupt's vineyard and also a crop mortgage on the growing grapes and on subsequent grape crops to be grown. The respondent claims that because of these mortgages it is not only entitled to the net proceeds—after the necessary expenses of harvesting the grapes and taking care of the vineyard have been deducted —but to the gross proceeds derived from the sale of the

grapes. This is an attempt to gain unjust enrichment at the expense of the Conciliation Commissioner.

Counsel for respondent attempts to sustain that position on highly legal technicalities. He utterly fails to understand the aims and purposes of Section 75 of the Bankruptcy Act. He assumes that a mortgage is a sacred obligation. He forgets that every mortgage or contract is subject to the Constitution and the laws enacted under its provisions.

Counsel forgets that in a bankruptcy proceeding the Court takes full and complete, and not only partial, jurisdiction over all of the property of the debtor. He forgets that then a mortgage contract is no more sacred than any other kind of contract or obligation. One and all are merged into the bankruptcy proceeding.

Nothing Divine About a Mortgage.

Under the present and previous Bankruptcy Acts the courts have always had jurisdiction over encumbered property. It is true that these Acts generally preserved for the mortgagee or lien holder the right to recover the net proceeds or value of the property upon which he held a lien, but the right of the Court to assume jurisdiction and control over the property itself has always existed and exists now by specific Acts of Congress. (Sections 74, 75, 77 and 77B.)

> "The fact that secured debts are affected by the act does not, of course, raise any grave constitutional question, and can be dismissed with brief comment. *'A secured debt or lien is, so far as the Constitution of the United States is concerned, a no more sacred kind of property than an unsecured debt, • • • and the Constitution expressly permits and grants to Congress the power to affect such property, whether it be an unsecured debt or whether it be a lien, by laws relating to the subject of bankruptcies.' In re Burgh,* 7 Fed. Supp. 184, 185; *Continental Ill. Nat. Bank and Trust*

Co. v. *Chicago, Rock Island and Pacific Ry.*, 294 U. S. 648; *Campbell* v. *Alleghany Corporation*, 75 F. (2d) 947."

Conciliation Commissioner's Powers and Duties.

As we have seen, the jurisdiction and powers and duties of the District Court and the Conciliation Commissioner, over agricultural compositions and extensions, are set forth in Section 75 and more particularly, as far as this case is concerned, in Subsections (e) and (n).

> "(e) * * * After the filing of the petition and prior to the confirmation or other disposition of the composition or extension proposal by the court, *the court shall exercise such control over the property of the farmer as the court deems in the best interest of the farmer and his creditors.*"
>
> "(n) *The filing of a petition pleading for relief under this section shall subject the farmer and his property, wherever located, to the exclusive jurisdiction of the court.* In proceedings under this section, except as otherwise provided herein, *the jurisdiction and powers of the court, the title, powers, and duties of its officers, the duties of the farmer, and the rights and liabilities of creditors, and of all persons with respect to the property of the farmer and the jurisdiction of the appellate courts, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the farmer's petition or answer was filed.*"

In the case at bar the petitioner, Noah Adair, as Conciliation Commissioner, was compelled to pay for the harvesting of the grapes. The farmer-debtor was financially unable to do so. Grapes are a perishable commodity. If they had not been promptly harvested they would have been lost to the estate. The vineyard had to be taken care of to assure future crops. The undisputed evidence shows that the petitioner paid no more than was absolutely necessary to conserve and protect the estate and the mortgaged prop-

erty for the respondent and other creditors (R. 13-16 and 25-27).

All the items paid by the petitioner, except $22.50 to a court reporter, $50.00 for attorney's fees and $20.00 for filing fees, were paid to laboring men for services and to the farmer-debtor for living and other necessary expenses in connection with and while harvesting the grapes and taking care of the vineyard (R. 8 and 22).

All these payments were approved and OKed by the referee in bankruptcy (R. 27). They were allowed and approved by the District Court after hearing, at which hearing the respondent was present (R. 29).

As we have stated, under Section 75 the Conciliation Commissioner, like a referee in bankruptcy, is an officer of the Court and in addition he and the farmer-debtor take the place of a trustee in bankruptcy, and expenses incurred in the actual care and preservation of the property must be provided for to the postponement, if necessary, of all other charges. (Sec. 302, Black on Bankruptcy (2d); *In Re Mitchell*, 129 C. C. A. 452.)

Before Section 75.

Even before Sections 64, 75, 77 and 77B were enacted the trustee in bankruptcy had power to conserve property belonging to the estate and to continue the business for a limited period and charge the necessary expenses of doing so to the estate regardless of secured or unsecured creditors. It is true that prior to these Sections, the courts first paid the expenses out of the unsecured assets, but when those were exhausted it did not hesitate to pay them out of the secured assets. All that Congress did in these Acts was to provide a uniform rule and fix the rights of the debtor and creditors more definitely, and in doing so it intended to give the debtor an opportunity to be rehabilitated.

> "67. Contracting indebtedness.—A receiver who is authorized to conduct a business, for the successful con-

duct of which it is necessary and customary to receive credit and borrow money; has the implied power to purchase on credit and even to borrow money; where the power is expressly conferred by the court the limitations imposed must be observed." G. Coll. 3 Ed., 51.

"1216. Sums paid for preservation of property.—*The trustee may be allowed for all sums necessarily paid for the preservation of the estate.* If such sums have been paid by other parties he may with the approval of the court, repay them, especially if they had an interest in the preservation of the property, *and if there were circumstances which necessitated prompt action on their part.* Thus, if creditors prior to the appointment of a trustee should pay for liens which were being enforced in order to save the property for the estate they would be subrogated to the rights of the lienors. Where expenses are incurred by a trustee in the preservation of property subject to mortgage, solely in the interest of creditors generally, they should be paid out of the state, and may not be charged against the mortgagees." G. Coll. 3 Ed., 930.

"*Moneys spent by the trustee, with full knowledge of lien creditors, to preserve the estate are chargeable against proceeds of sale and payable prior to liens on the estate.* Virginia Securities Corp. *v.* Patrick Orchards, Inc. (C. C. A., 4th Cir.), 20 F. (2d) 78." G. Coll. 3 Ed., 930.

"1304. In general.—Subdivision 1 of Subsection b provides as the first statutory priority that there shall be paid "*the actual and necessary cost of preserving the estate subsequent to filing the petition.*" The words of this subdivision give priority to the (1) actual and (2) necessary cost (3) of preserving the estate (4) subsequent to filing the petition." G. Coll. 3 Ed., 1020.

"* * * If the business is so carried on by the trustee, *he should be required to pay all bills promptly if legitimately contracted by him in the business including the wages of skilled employees whom it is necessary to retain* as being the only persons acquainted with the

business. * * *" 181 Blk. Bkr. 2d Hornbook, 423.

"Allowance for Expenditures.—Expenditures by a trustee in bankruptcy, to be allowed by the court, must have been actually made, *reasonably necessary, and beneficial to the estate. The trustee is allowed to incur all necessary expenses for the care and custody of the bankrupt's property while in his hands, including the care and pasturage of sheep or stock.* * * * He may and should pay all taxes assessed or becoming due on the bankrupt's property while it is in his hands, including customs duties on imported merchandise, in order to obtain its release from bond. The Estate must also bear the cost of actions or proceedings properly undertaken by the trustee for the purpose of recovering assets or contesting spurious claims, but he will not be allowed the costs of unfounded and unnecessary litigation. * * * An expenses incurred exclusively for the benefit of a particular creditor or creditors cannot be charged to the estate in general.

"Employment and Compensation of Counsel.—* * * But on the other hand, where the situation of the estate is such that he really requires legal assistance, the trustee may employ counsel, and their fees for services properly and actually rendered to the trustee, to a reasonable amount, may be allowed as part of the costs of administration. * * *" 184 Blk. Bkr. 2d Hornbook, 431.

Same Power as Receiver and Trustee.

As a matter of fact a Conciliation Commissioner in bankruptcy occupies the same position as a referee in bankruptcy. The property is under the control of the Court. The farmer is permitted to continue in business with a view of rehabilitation. The Conciliation Commissioner supervises that possession and together with the farmer they have the same powers and duties as a receiver in a receivership or a trustee in a trusteeship.

"In General.—The general rule is, that the expenses of properly administering a trust are a lien, on behalf

of the trustee, on the estate in his hands, *and he will not be compelled to part with his control of that estate until such expenses are paid; nor does the right of reimbursement depend on the knowledge or consent of the cestui que trust.* Trustees invested with general powers of control and management are not bound to strict limitations; they are justified in making ordinary repairs and improvements and insuring the property. The duty of a trustee, whether of real or personal estate, to defend the title, at law or in equity, in case a suit is brought against it, is unquestioned, and the expenses are properly chargeable against the estate." 26 R. C. L. 1320, par. 179.

"* * * But where trustees have in good faith expended moneys under an invalid trust which they believed to be valid they cannot be compelled to account therefor to those who have long stood by and allowed the expenditures without objection. * * *" 26 R. C. L. 1387, par. 252.

"Credits.—A trustee who is compelled to account to his *cestui que* trust is entitled to credit for the sums *expended by him in the acquisition of the trust property, and for its protection and preservation,* and he is also entitled to a credit for interest on advances made for the use of the *cestui que* trust, to an allowance for depreciated money paid for rent of the trust estate, and for expenses incurred in erecting necessary and proper buildings. * * * The duty of a trustee, whether of real or personal estate, *to defend the title, at law or in equity,* in case a suit is brought against it, is unquestioned, and the expenses thus incurred are properly chargeable in his accounts against the estate. * * *" 26 R. C. L. 1389, par. 254.

"* * * If the mortgaged property is used for business purposes, the court may authorize the receiver to carry on the business. Having such authority, all debts incurred by him in carrying on the business for which the property is used, such as operating a mill, take precedence of the mortgage debt. Where the receiver incurred expenses that would necessarily

have been made by the mortgagee had he remained in possession of the premises, in order to make the same yield rent, such receiver will be allowed to retain from the rents collected the amount of his disbursements. His possession is the possession of the court, and without its authority no one can directly or indirectly interfere with the property. Like a trustee, he is bound to exercise such care over the property as a prudent man would take of his own. A receiver who acts in good faith, but under a mistake as to the extent of his powers, is not, it would seem, liable for his acts." Jones on Mortgages, 8 Ed., 436, par. 1951.

Approval of Court.

It is contended that the Conciliation Commissioner should not have harvested the grapes without an order of the Court. It is also contended that he should not have paid for the harvest without an order. But even if this were true, when the United States District Court approved and allowed these expenditures, then the acts of the Conciliation Commissioner, its appointed officer, became the acts of the Court. By its approval the Court made the Conciliation Commissioner's acts its own. If the Court could give the order in the first place, it could give it by approval afterwards. *Pneumatic Scale Corporation, Limited,* v. *Mainwaring,* 286 Fed. 378; *Thompson-Starrett Co.* v. *La Belle Iron Works,* 17 F. (2d) 536.

Going Concern.

A farm is a going concern. Section 75 of the Bankruptcy Act continues it as a going concern. At the time that the debtor here filed, the original Subsection (s) was part of Section 75. It provided the method by which the farm could be continued as a going concern for a term of five years. When Subsection (s) was held unconstitutional the new Subsection (s) was added. This has been held con-

stitutional. It provides the method of procedure for continuing the farm as a going concern for three years with a view of rehabilitating the farmer.

The total value of the farmer-debtor's estate on the day of filing his petition under Section 75, consisted of $22,500 real estate and $1,370 of household goods and other exempt property. He had no cash on hand (R. 2). The respondent had a mortgage on the real estate and on the crop of grapes growing and on subsequent crops (R. 4 and 28). There were no other funds or other property with which to pay the expenditures made on behalf of the estate. All of the expenditures were incurred prior to the dismissal on October 14, 1935. The respondent received $1,600, the proceeds from the crop of 1935 (R. 78).

Conclusion.

From the above it is clear that the District Court had jurisdiction of the farmer-debtor and over his property from August 4, 1934, to October 14, 1935, when the debtor's petition was dismissed. But the Court again assumed jurisdiction on March 16, 1936, when it reinstated or permitted the debtor to refile his petition.

In closing may we respectfully refer this Court to our brief in support of the petition for writ of certiorari beginning with page eleven. The decision of the Circuit Court of Appeals should be reversed and the District Court's decision reinstated.

Respectfully submitted,

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RESPONDENT'S REPLY TO BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

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